

City Light System

Power Resources. The Department owns and operates three major hydroelectric generating plants on the Skagit River, approximately 80 miles northeast of Seattle, and the Boundary Hydroelectric Plant (the “Boundary Project”) on the Pend Oreille River, approximately 250 miles east of Seattle. In addition, the Department owns three smaller hydroelectric plants in western Washington. The Department sold its eight percent share of the coal-fired Centralia Steam Plant to TransAlta Corporation in May 2000.

In addition to these resources, the Department’s power is supplied through contracts with Bonneville, two public utility districts and three Columbia Basin irrigation districts. Additional contracts are in place with King County, the Province of British Columbia, the City of Klamath Falls, Oregon, three Idaho irrigation districts, and one Oregon irrigation district. A long-term contract for the purchase of power from a wind-powered generation project in the Northwest region has been signed with PacifiCorp Power Marketing, Inc. (“PPM”).

More detailed information on the Department’s power resources is provided under “Power Resources” below.

Transmission Facilities. The Department operates a system of 656 miles of transmission facilities that follow several routes. Power from the Skagit River plants is transmitted over lines owned by the Department. The Department also uses the facilities of other agencies, principally Bonneville, to transmit power from other generating plants from which the Department receives power, including the Boundary Project. The Department’s transmission facilities are connected to Bonneville’s transmission grid. The Department also has acquired ownership rights to 160 MW of capacity over the AC Intertie, which connects the Pacific Northwest power grid with the Southwest region. See “Power Resources—Transmission.”

Distribution Facilities. There are 14 major substations in the Light System. Service in the City’s downtown business area and other areas of high load density is provided through underground network systems.

General Plant. The Department’s general plant facilities include two service centers that serve as headquarters for construction and maintenance activities, the System Control Center, communication facilities, transportation equipment, and office equipment, including data processing equipment. The System Control Center, completed in 1995, houses an advanced energy management system. The Department’s central administrative offices are located in Key Tower, a downtown Seattle office building owned by the City.

Taxation and Intergovernmental Payments

The Department pays a utility tax to the City equal to six percent of Gross Revenues from sales within the State. The proceeds of this tax are deposited into the City’s General Fund. The City Charter does not permit the Department to pay taxes to the City’s General Fund “until ample provision has been made for the servicing of the debts and obligations of the utility and for necessary betterments and replacements for the current year.” A State public utility tax is paid at a rate of 3.873 percent of Gross Revenues from sales within the State, less certain adjustments.

Certain contractual payments are made to Pend Oreille and Whatcom Counties, Washington, for services rendered. Under the terms of franchise agreements signed in 1998 and 1999, the Department makes monthly payments to the cities of Shoreline, Burien, Lake Forest Park, and SeaTac in amounts equal to six percent of the revenue attributable to the energy component of rates charged to customers residing within those cities. In April 2003, the Department signed a franchise agreement with the City of Tukwila that requires the Department to pay the City of Tukwila monthly amounts equal to four percent of the revenue billed to customers in Tukwila. See “The Department—Retail Rates.”

Retail Rates

Rate Setting. The City Council has exclusive jurisdiction with respect to establishing and revising the Department’s retail rates. State law requires that rates must be fair, nondiscriminatory and fixed to produce revenue that is adequate to pay operation and maintenance expenses of the Department and to meet all debt service requirements payable from such revenue. In its retail rate-setting capacity, the City Council is not

subject to control by the Washington Utilities and Transportation Commission, but it is subject to certain rate-making provisions of the Public Utility Regulatory Policies Act of 1978. The Department never has been cited for failing to comply with such act, and believes that it is operating in compliance with the act's requirements.

Since 1980 the City Council has conducted comprehensive reviews of the Department's rate levels and rate structure at intervals of two or three years. In the course of its rate reviews, the City Council holds public meetings to consider the Department's proposed budget, construction plan, load forecast, and resource plans. Based on these planning documents, as approved by the City Council, the Department's staff estimates the Department's revenue requirements and develops a rate proposal that will produce the required amount of revenue and that allocates the revenue requirement among the various rate classes in accordance with City policy. The City Council holds public meetings to introduce and explain the proposals to the public and to accept public input. The City Council makes final decisions through passage of a rate ordinance.

Rate Changes: 1990-1999. From 1990 through 1999, the City's periodic rate reviews resulted in the following changes in average rates for the system as a whole:

SUMMARY OF RATE CHANGES 1990-1999

<u>Effective Date</u>	<u>Percentage Change</u>
January 1, 1990	(2.4)%
May 1, 1993	12.6
March 1, 1995	5.7
March 1, 1996	5.3
March 6, 1997	(0.4)
March 1, 1998	(0.6)
December 24, 1999	3.2

In addition to these changes, the City Council imposed three temporary surcharges ranging from 4.1 percent to 10.0 percent between 1992 and 1995 to offset the impact of poor water conditions on power costs.

The most recent comprehensive rate review took place in 1999 and culminated in the passage of an ordinance in November 1999 that provided for an average increase of 3.2 percent, effective December 24, 1999. Pursuant to City policy, rates for low-income residential customers were set at levels 50 percent below rates in the standard residential classes. The ordinance provided for a further increase averaging 3.0 percent, effective March 1, 2002.

Rate Changes: 2000-2003. In 2000 and the first nine months of 2001, the Department was required to purchase large amounts of power in the wholesale market as a result of its 1996 decision to limit purchases of power from Bonneville (see "Power Resources—Purchased Power Arrangements"), the sale of the Centralia Steam Plant in May 2000 and unusually poor water conditions in the water year beginning October 1, 2000. Beginning in May 2000, largely as a result of supply constraints and the repercussions of restructuring efforts in California, wholesale market prices increased to unprecedented levels. As a result, the Department incurred power expenses in 2000 and 2001 that in total exceeded its budgeted estimates by almost \$600 million. See "Change in the Electric Utility Industry," "Recent Developments Affecting the Department" and "Historical and Projected Operating Results." In response to these developments, the City increased rates four times in 2001:

- (i) Effective January 1, 2001, all energy charges were increased by 0.4 cents per kWh, with the exception of rates for low-income customers, which were increased by 0.2 cents per kWh. On the average, rates increased by 9.8 percent.
- (ii) Effective March 1, 2001, winter energy charges for all classes except the low-income classes were increased by 0.4 cents per kWh and the distinction between summer rates and winter rates was eliminated. Rates for low-income customers remained unchanged. With rates for non-low-income

customers set at the higher winter levels in all months of the year, average rates increased by 18.0 percent.

- (iii) Effective July 1, 2001, energy charges for all classes except the low-income classes were increased by 0.49 cents per kWh, which represented an increase of 9.3 percent in average rates. Average rates for low-income customers were not increased, but effective October 1, 2001, the distinction between summer and winter rates for low-income customers was eliminated, and rates were set at the average of winter and summer rates.
- (iv) Effective October 1, 2001, all energy charges were increased by 0.6 cents per kWh, or 10.3 percent, with the exception of energy charges for the low-income rate classes, which received an increase of 0.3 cents per kWh. This increase passed through to customers the financial effect of increases in rates charged by Bonneville for transmission services and power purchases. Pass-through of the October 1, 2001, transmission and power rate increases had been mandated by the ordinances implementing the December 24, 1999, rate increases and the July 1, 2001, power cost adjustment, respectively. See “Power Resources—Purchased Power Arrangements.”

The last of the rate ordinances in 2001 also required that the effect of future increases or decreases in Bonneville rates be passed through to customer classes through adjustments to their energy charges. Pursuant to this provision, energy charges for all rate classes were reduced by 0.07 cents per kWh, effective April 1, 2002, except for the low-income rate classes, which were reduced by 0.04 cents per kWh. This resulted in an average decrease of 1.1 percent. Further rate adjustments by Bonneville were passed through to City Light customers on April 1, 2003, through an increase of 0.08 cents per kWh in energy charges for all classes except the low-income classes, which received an increase of 0.04 cents per kWh. The average rate increase on April 1, 2003, was 1.2 percent.

In addition to the four power cost adjustments enacted in 2001, rates for Medium and Large General Service customers in the downtown network were increased by 4.1 percent and 3.8 percent respectively, effective March 1, 2002, as provided for in the November 1999 rate ordinance. Fees for rental of streetlights, poles, ducts, and vaults also increased on that date. These increases resulted in an average increase of 0.5 percent for the system as a whole. The ordinance enacting the power cost adjustment effective July 1, 2001, eliminated the increases for the other rate classes that were to have taken effect on March 1, 2002, under the terms of the November 1999 ordinance.

Under the terms of the April 2003 franchise agreement between the City of Tukwila and the Department, customers in the City of Tukwila received rate increases averaging 4.7 percent to 5.6 percent, depending on the rate class, effective May 1, 2003. See “The Department—Rates Outside the City of Seattle.”

SUMMARY OF RATE CHANGES SINCE JANUARY 1, 2000

<u>Effective Date</u>	<u>Percentage Change</u>
January 1, 2001	9.8%
March 1, 2001	18.0
July 1, 2001	9.3
October 1, 2001	10.3
March 1, 2002	0.5
April 1, 2002	(1.1)
April 1, 2003	1.2
May 1, 2003	0.2

The net effect of the four power cost adjustments in 2001, the March 1, 2002, increase in network rates, the pass-through of the Bonneville rate adjustments on April 1, 2002, and April 1, 2003, and the increase in Tukwila rates has been to increase average rates for the system as a whole by 57 percent. Because low-income rates were exempted from the power cost adjustments effective March 1, 2001, and July 1, 2001, rates for low-income customers increased by about 20 percent.

Under the terms of the financial policies adopted by the City Council for the Department in December 2001, current rates will remain in effect until the Department repays all short-term debt obligations, including the 2002 Notes and the amounts borrowed from the Cash Pool, and accumulates an operating account cash balance of \$30 million, unless rates are increased by City Council action or adjusted to pass through further changes in Bonneville power rates. These conditions are expected to be met in mid-2004. At that point rates can be set in accordance with the rate-setting guidelines in the City Council-adopted financial policies, which give greater recognition to the higher risks that the Department faces in the current utility environment. The Department's financial forecast assumes that new rates will take effect on January 1, 2005. Financial policies adopted by the City Council are subject to change by the City Council. See "The Department—Financial Policies."

In 2002, the Department's average rate for residential service was 6.90 cents per kWh. The Department's commercial and industrial rates averaged 6.20 cents and 5.28 cents per kWh, respectively. See the table titled "Average Rates and Monthly Bills" for average rates and bills paid by the various customer classes. With the Department's recent power cost adjustments taken into account, the Department's current average rates are below the national average. See the table titled "Annual Bill Comparisons with Other Puget Sound Utilities" for a comparison of annual amounts paid by the Department's customers and the customers of neighboring utilities.

Rates Outside the City of Seattle. In 1998 and 1999, the cities of Shoreline, Lake Forest Park, SeaTac, and Burien granted franchises to the Department which recognized the right of the Department to set higher rates for customers located in those cities than the rates charged to Seattle customers. However, the differential between rates in Seattle and rates outside Seattle was limited to eight percent of the energy portion of rates, plus amounts required to recover the cost of service levels requested by any of the suburban cities that exceeded standard service levels provided by the Department. The rate ordinance that took effect in 1999 set rates for customers in these cities and in unincorporated King County at the maximum level permitted under the franchises. The franchise agreement then in effect between the Department and the City of Tukwila required the Department to charge the same rates in Tukwila as in Seattle. In April 2003, Tukwila granted a new franchise which contained rate provisions similar to those in the franchises with the other suburban cities. Rates in Tukwila were increased effective May 1, 2003.

Market-Indexed Rates for High Demand Customers. Since 1996, the Department has offered market-indexed rate schedules ("Market-Indexed Schedules") to the eight customers in its High Demand General Service classes. Currently no customers are served under the Market-Indexed Schedules.

Special Rates for New Large Loads. The City Council passed an ordinance in 2000 that created a new customer class for New Large Loads. A New Large Load is defined in the ordinance as any service fed from an expanded or a new installation equal to or greater than 12.5 megavolt-amperes ("MVA") of energized capacity installed within any consecutive five-year period after August 31, 2000. The ordinance provides that New Large Load customers will be charged for service either under the Department's Market-Indexed Schedule (see "The Department—Retail Rates—Market-Indexed Rates for High Demand Customers") or on the basis of a negotiated, customized delivery and payment package which would include one of a number of options for acquiring and paying for energy. New Large Loads will also pay a retail service charge to the Department for delivery of power to the customer's premises. Under either payment option, each New Large Load customer is responsible for installation costs and a fixed charge per MW of capacity to cover the cost of providing feeder and substation capacity. Currently no customers are being served as New Large Loads.

Interruptible Rates for High Demand Customers. In 2001, the City Council passed an ordinance creating a new rate class for High Demand General Service customers that sign contracts with the Department for interruptible service. Under the terms of such contracts, the Department has the right to interrupt service to such customers when the wholesale market price of energy exceeds a "trigger price," which has been set at \$55 per MWh through the end of 2003 and may be adjusted by the Department after that date. Through December 31, 2003, rates for High Demand customers choosing to be served on this basis have been set at levels approximately 30 percent below the rates for standard High Demand customers. Effective January 1, 2004, rates for this class will be the standard rates for customers in the High Demand class in the City of Seattle, plus 0.725 cents per kWh. This additional charge will remain in effect until the customer has

consumed five times the amount of energy actually consumed in calendar year 2000. One customer has signed a contract with the Department for interruptible service.

Voluntary Green Power Program. Pursuant to State law, the Department provides residential customers the option of paying additional monthly amounts of \$3, \$7 or \$10 to fund renewable resources. Non-residential customers also can elect to make voluntary payments in amounts ranging from \$8 to \$150 per month. The proceeds of these voluntary payments will be used by the Department to fund the acquisition of energy from renewable resources, such as solar, wind, fuel cells, and landfill gas. See “Power Resources—Purchased Power Arrangements—Other Renewable Resources.” As of January 1, 2003, 3,470 customers had elected to participate in the program.

AVERAGE RATES AND MONTHLY BILLS

	Average Revenue in Cents per kWh				Average Monthly Bills			
	City Standard	City Network	Suburban ⁽¹⁾	City of Tukwila	City Standard	City Network	Suburban ⁽¹⁾	City of Tukwila
Residential								
500 kWh per month	5.9		6.0	6.2	\$29		\$30	\$31
1,000 kWh per month	7.3	(2)	7.4	7.6	73	(2)	74	76
2,000 kWh per month	8.0		8.1	8.3	159		161	166
Small General Service								
10,000 kWh per month (40kW)	6.1	(2)	6.2	6.4	\$613	(2)	\$624	\$643
Medium General Service								
20,000 kWh per month (60kW)	6.2	6.9	6.4	6.6	\$1,250	\$1,381	\$1,272	\$1,312
200,000 kWh per month (500kW)	6.2	6.8	6.3	6.5	12,395	13,655	12,615	13,015
Large General Service								
400,000 kWh per month (1,000kW)	5.8	6.3	5.9	6.1	\$23,260	\$25,109	\$23,619	\$24,327
1,800,000 kWh per month (5,000kW)	5.8	6.3	5.9	6.1	104,868	113,408	106,486	109,782
High Demand General Service								
6,000,000 kWh per month (20,000kW)	5.6	(3)	(3)	5.9	\$335,642	(3)	(3)	\$356,529
18,000,000 kWh per month (60,000kW)	5.6			5.9	1,006,925			1,069,587

(1) All jurisdictions outside the City of Seattle, except the City of Tukwila.

(2) There are no separate rate schedules for Residential and Small General Service customers located within the network.

(3) All High Demand General Service customers are located in Seattle or Tukwila.

**ANNUAL BILL COMPARISONS WITH OTHER PUGET SOUND UTILITIES
(BASED ON RATES IN EFFECT ON APRIL 1, 2003)**

Monthly Use		Seattle City Light				Puget Sound Energy (4)	Snohomish County PUD	Tacoma Power
kWh	kW	City Standard	City Network	Suburban ⁽¹⁾	City of Tukwila	City of Bellevue	City of Everett	City of Tacoma
Residential								
100		\$87		\$88	\$91	\$128	\$162	\$135
500		352	(2)	358	372	364	493	411
1,000		872		884	911	742	985	757
3,000		2,950		2,986	3,069	2,334	2,956	2,138
Small General Service								
300	1	\$221		\$225	\$231	\$427	\$377	\$325
3,000	10	2,207	(2)	2,246	2,315	2,727	2,790	2,276
12,000	40	8,827		8,986	9,259	10,394	10,831	8,782
Medium General Service								
150,000	500	\$113,100	\$125,280	\$115,080	\$118,680	\$131,604	\$121,546	\$90,425
200,000	500	148,740	163,860	151,380	156,180	162,886	156,721	109,663
360,000	900	267,732	294,948	272,484	281,124	292,901	278,359	196,952
Large General Service								
300,000	1,000	\$210,665	\$228,281	\$213,662	\$220,142	\$228,586	\$219,826	\$180,299
1,000,000	5,000	710,154	778,966	720,949	742,549	864,986	790,647	706,908
2,500,000	7,500	1,751,568	1,893,955	1,776,513	1,830,513	1,831,966	1,802,939	1,444,842
High Demand General Service								
6,000,000	20,000	\$4,027,700			\$4,278,350	\$3,609,265	\$4,396,524	\$3,595,488
18,000,000	60,000	12,083,101	(3)	(3)	12,835,049	10,827,794	13,189,572	10,785,360
24,000,000	60,000	16,018,024			17,022,972	13,734,515	16,891,380	13,093,896
Last Rate Change		4/01/03	4/01/03	4/01/03	5/01/03	2/15/03	10/01/02	3/31/03

(1) All jurisdictions outside the City of Seattle, except the City of Tukwila.

(2) There are no separate rate schedules for Residential and Small General Service customers located within the network.

(3) All High Demand General Service customers are located in Seattle or Tukwila.

(4) For Puget Sound Energy, Large General Service is Primary General Service and High Demand General Service is High Voltage General Service.